



November 19, 2004

VIA E-MAIL

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, D.C. 20551

RE: Docket No. R-1210

Dear Ms. Johnson:

The following comments are submitted on behalf of ACA International (“ACA”) in response to the request by the Federal Reserve Board (“FRB”) for comments regarding amendments to Regulation E and the Official Staff Interpretation on Regulation E.¹ Pursuant to the request for comment, the FRB seeks to amend Regulation E and its Official Staff Interpretation to address issues related to electronic check conversion transactions, payroll accounts and preauthorized transfers. ACA’s comments will focus on the proposed amendments regarding electronic check conversion transactions and the electronic collection of service fees for dishonored checks and electronic funds transfers.

ACA International is an international trade organization of credit and collection professionals who provide a wide variety of accounts receivable management services. Founded in 1939 and headquartered in Minneapolis, Minnesota, ACA represents approximately 5,300 members. A subset of these members present and collect checks both electronically and in paper form, conduct electronic transactions, and collect service fees for dishonored checks and electronic funds transfers (“EFTs”). As such they are required to comply with numerous federal and state laws and regulations, including two conflicting regulations, Regulation E and the Operating Rules of the National Automated Clearing House Association (“NACHA”).

Merchants and creditors will contract with ACA member collection agencies to present and collect checks. Typically, a consumer will write a check at the point of sale. The merchant either will take the paper check or convert the check into an EFT at the point of

¹ See Notice of Proposed Rulemaking, 69 Fed. Reg. 55996 (Sept. 17, 2004) (“NPRM”).

sale. Then the merchant will present the paper checks to its financial institution or hire one of our members to process the checks. If the merchant presents its own checks, any checks that are returned dishonored are forwarded to a collection agency for collection. The same is true for dishonored EFTs. The collection agency will re-present the check as an RCK transaction through the automated clearing house (“ACH”) network or re-present the paper check to the financial institution. In addition, the collection agency will attempt to collect a service fee for any dishonored checks or EFTs if such fee is permitted by state law. Our members process and collect hundreds of thousands of checks each month totaling millions of dollars per year.

The problem that arises for our members is that Regulation E and the NACHA Operating Rules have conflicting requirements for carrying out the various transactions described above. In order to convert a check into an EFT at the point of sale, Regulation E states authorization occurs when a consumer receives notice the check will be converted and goes forward with the transaction.² For the same transaction, the NACHA Operating Rules require the merchant to obtain the written authorization of the consumer.³ In order to collect a service fee electronically for the dishonored check under Regulation E, the consumer authorizes the transaction when he or she is provided notice that the fee will be collected electronically and goes forward with the transaction.⁴ The NACHA Operating Rules require the prior written authorization of the consumer in order to electronically debit his or her account for the amount of the service fee.⁵ Regulation E does not apply to the electronic re-presentation of a returned check because the transaction originated by paper check.⁶ NACHA, on the other hand, requires notice be provided to the consumer at the time the check is written.⁷

Due to contractual relationships with third-party service providers and financial institutions, our members are required to comply with the NACHA Operating Rules.⁸ Because Regulation E is a federal regulation, ACA members are also required to comply with Regulation E. The conflicting provisions of Regulation E and the NACHA Operating Rules have created an unlevel playing field for the members of ACA. It is ACA’s understanding there is an industry segment that does not comply with the NACHA Operating Rules as they believe NACHA does not have the authority to enforce contractual provisions in contravention of federal regulations. Other segments of the industry remain confused by the conflict between Regulation E and the NACHA Operating Rules and are compelled to attempt to comply with both, which causes them to have higher operating costs than the segment not complying with the NACHA rules. The segment complying only with Regulation E is able to collect checks and the applicable service fees more quickly and efficiently.

² 12 C.F.R. § 205.3(b)(2)(i); Official Staff Interpretation on Regulation E Comment § 205.3(3)(b)(2)-1.

³ NACHA Operating Rule 2.1.2.

⁴ Official Staff Interpretation on Regulation E Proposed Comment § 205.3(3)(c)(1)-1.

⁵ NACHA Operating Rule 2.1.2.

⁶ Official Staff Interpretation on Regulation E Comment § 205.3(3)(c)(1)-1.

⁷ NACHA Operating Rule 2.1.4.

⁸ NACHA Operating Rule 2.1.1.

Further, there has been a complete lack of enforcement by NACHA with regard to their own rules. This has led to lawsuits against collection agencies that allegedly collected a service fee electronically for a dishonored check based on a point of sale sign. Although the point of sale sign satisfies the requirements of Regulation E, the agencies are not obtaining the written authorization of the consumer as required by the NACHA Operating Rules. To date, these cases are still being litigated and the industry continues to operate without clear direction. It is important to note, courts are not responsible for making the law, it is their duty to interpret the law. Since the law remains unclear, ACA opines the FRB has a duty to clarify the law so that the parties have a clear understanding of their obligations under the law.

In order to level the playing field and minimize further litigation based on the inconsistencies between Regulation E and the NACHA Operating Rules, ACA urges the FRB to adopt a provision in Regulation E stating that any contractual agreements which conflict with Regulation E are deemed unenforceable, contrary to public policy, and serve to undermine a consistent electronic transaction model. NACHA should not be allowed to mandate additional authorization requirements in addition to and in contravention of Regulation E.

In addition, ACA requests the FRB to: (1) further clarify that authorization for the electronic debiting of a consumer's account for the amount of the service fee for a dishonored check or EFT occurs when the consumer has received notice of such and goes forward with the transaction; (2) maintain the present regulation that notice provided to the consumer is sufficient authorization for converting a check into an EFT at the point of sale; and (3) modify the proposed notice requirements and model notices to place the onus on financial institutions to provide notice regarding the speed at which EFTs are debited from consumer accounts and that checks will no longer be returned by financial institutions.

I. ACA requests the FRB to further clarify that authorization for the electronic debiting of a consumer's account for the amount of the service fee for a dishonored check or EFT occurs when the consumer has received notice of such and goes forward with the transaction.

The FRB is seeking to adopt a new provision in the Official Staff Interpretation on Regulation E regarding the electronic collection of service fees for dishonored checks and electronic funds transfers.⁹ The comment states that the electronic collection of such fees is covered by Regulation E and must be authorized by the consumer.¹⁰ However, the comment does not clarify that notice equals authorization. ACA urges the FRB to clarify that notice equals authorization in electronically debiting a consumer's account for the amount of the service fee for a dishonored check or EFT and thereby resolve the conflict between Regulation E and the NACHA Operating Rules.

⁹ Official Staff Interpretation on Regulation E Proposed Comment § 205.3(3)(b)-3.

¹⁰ *Id.*

Again, the NACHA Operating Rules are in direct conflict with this requirement. NACHA requires written authorization in order to electronically debit a consumer's account for a service fee for a dishonored check or EFT.¹¹ Those parties that are not complying with this provision of the NACHA rules are able to collect the service fees faster and more efficiently than those parties who are obtaining the written authorization. The parties who are complying with the NACHA rules are losing business to those parties who are simply following the requirements of Regulation E. This has been an area of great frustration to our members. It seems as if NACHA has not made any effort to enforce their written authorization requirement, yet our members feel compelled to comply because of the contractual agreement they have with third-party service providers and financial institutions.

Specifically, ACA urges the FRB to clarify in comment 205.3(3)(b)-3 that the consumer authorizes the debiting of his or her account for the service fee for a dishonored check or EFT when the consumer receives notice as such and goes forward with the transaction. We ask the FRB to add the following sentences to the end of proposed comment 205.3(3)(b)-3: "Authorization occurs where the consumer has received notice that a fee imposed for returned checks and returned electronic funds transfers will be debited electronically from the consumer's account and goes forward with the transaction. Examples of notice include, but are not limited to, signage at the point of sale or individual written statements provided to consumers." This language clarifies that notice equals authorization and describes what constitutes notice. ACA again urges the FRB to resolve this issue in favor of a notice requirement to the consumer at the point of sale.

II. ACA requests the FRB to maintain the present regulation that notice provided to the consumer is sufficient authorization for converting a check into an EFT at the point of sale.

The FRB is seeking comment regarding whether Regulation E should adopt a written authorization requirement for converting checks into EFTs at the point of sale. While written authorization is currently required by the NACHA Operating Rules,¹² the FRB should not adopt a similar requirement.

Under the NACHA Operating Rules, when a merchant wants to convert a check at the point of sale, the merchant must obtain the written authorization of the consumer, convert the check, and then return the paper check to the consumer. While ACA applauds the FRB's efforts to provide merchants the choice of converting the check into an EFT at the point of sale or processing the check,¹³ the NACHA Operating Rules effectively take away this option because merchants are required to convert immediately upon the check being tendered at the point of sale. Again, this is in direct conflict with the requirements of Regulation E. Only those parties accepting checks in a lockbox environment would be

¹¹ NACHA Operating Rule 2.1.2.

¹² NACHA Operating Rule 2.1.2.

¹³ Official Staff Interpretation on Regulation E Proposed Comment § 205.3(3)(b)(2)-2.

given the choice between converting the check or processing the check. Merchants at the point of sale should be afforded the same choice.

As many merchants contract with collection agencies to process their checks, collection agencies also need to have the option of converting the check into an EFT in order to effectively service their merchant clients. To avoid having to determine which check writers provided written authorization for conversion, merchants would need to adopt a policy that all check writers are required to sign the authorization for the merchant to accept the check. This is akin to coerced consent. Consumers who refuse to sign such an authorization would have to choose between not purchasing any items, using cash, or using a credit card.

The FRB should clarify in proposed comment 205.3(3)(b)(2)-2 that “clear authorization” occurs when the consumer receives notice that his or her check may be converted into an EFT or processed as a check and goes forward with the transaction. ACA would like the FRB to also make clear that examples of notice may include, but are not limited to, signs posted at the point of sale, notices in billing statements, or notices provided to consumers by financial institutions either when opening an account or in the financial institution’s annual disclosures.

A sign posted at the point of sale informing the check writer of the merchant’s conversion policy provides the same consumer protection as having the consumer sign a written authorization. Consumers are accustomed to reading signs posted at the point of sale and may turn to their financial institution for additional educational information about electronic transactions.

The purpose of industry regulation is not only to provide consumer with adequate protections, but equally important is the need to regulation to provide clarity and consistency to an industry. To allow other organizations to impose more stringent requirements on the very issues under the purview of the FRB undermines the FRB’s authority to create meaningful regulations and requires the system to rely on the courts to determine the applicable law or regulation. The FRB should therefore clarify that any contractual provisions in contradiction of Regulation E are unenforceable and in contravention of public policy. The FRB should not let other organizations dictate the operation of the electronic payments system, and therefore, undermine its integrity.

III. ACA urges the FRB to modify its proposed notice requirements and model notices to place the onus on financial institutions to provide notice regarding the speed at which EFTs are debited from consumer accounts and the return of checks by financial institutions.

The FRB is proposing several new notice requirements for merchants and payees. These new notice requirements would make the merchant or payee responsible for providing the notices to consumers and give the Federal Trade Commission (FTC) enforcement authority over these parties.¹⁴

¹⁴ 15 U.S.C. 1693o(c).

It is logical that the merchant or payee would be in the best position to provide notice informing consumers that their checks may be converted into EFTs or processed as checks. The payee has the most direct control over the transaction and the required notice. However, the FRB also wants merchants and payees to provide notice that when the consumer's check is converted, funds may be debited quickly and the check will not be returned by his or her financial institution. These are notices that are best provided by the consumer's financial institution, as the financial institution determines whether or not it will return checks to consumers. The same is true for the notice regarding the speed at which money will be debited from the consumer's account. With the advent of the Check Clearing for the 21st Century Act ("Check 21 Act"), a check may clear just as quickly if not quicker than an electronic transaction. Again, the consumer's financial institution is in the best position to provide this notice and the related consumer education materials. Such notices can be provided at the time a consumer opens an account with a financial institution or with the financial institution's annual disclosures and notices.

The FRB should allow at least one year from the date of adoption of any new notice requirements to comply with the new provisions. This will give merchants, collection agencies, and financial institutions sufficient time to modify existing point of sale signs, billing statements and annual disclosures as applicable.

IV. Conclusion

Signed authorizations do not provide any additional consumer rights than does a notice provided in a point of sale sign or a billing statement. Requiring different authorizations for different types of electronic transactions adds to consumer confusion and inconsistent handling of electronic transactions by the industry. By uniformly requiring notice as authorization, the FRB will consistently and uniformly institutionalize the electronic payments system, level the playing field among members of ACA, and perhaps most importantly, provide consumers with an electronic payment system upon which they may rely regardless of the individual merchant's policies.

The members of ACA International are operating on an unlevel playing field, created by NACHA. Contractually, our members are required to comply with the NACHA Operating Rules which are in direct conflict with Regulation E. In order to level the playing field, the FRB should adopt a provision stating that contracts in contravention of Regulation E are deemed unenforceable and contrary to public policy. The FRB should not allow another organization to develop rules for utilizing the electronic payments process. This undermines the authority of the FRB and the integrity of the electronic payments process. By adopting the position that Regulation E takes precedence over the NACHA Operating Rules, the FRB will make the electronic payments process more efficient and less confusing to consumers, as well as to those parties conducting electronic transactions.

The FRB should clarify that authorization to debit a consumer's account for the amount of a service fee for a dishonored check or electronic funds transfer occurs where the

consumer has received notice that the fee imposed will be debited electronically from his or her account and goes forward with the transaction. Examples of such notice include, but are not limited to, signs posted at the point of sale or written statements provided to consumers.

The FRB should not adopt a written authorization requirement for converting checks at the point of sale. The FRB should clarify that notice is sufficient authorization for conversion and that examples of notice include signs posted at the point of sale or written statements provided to consumers.

Finally, while merchants should be responsible for informing consumers as to the merchants' conversion policy, the onus should be on the financial institutions to educate consumers regarding the speed of electronic funds transfers and the financial institution's check return policy.

ACA appreciates the opportunity to comment on the FRB's proposed amendments to Regulation E and the Official Staff Interpretation on Regulation E. If you have any questions, please feel free to contact me.

Sincerely,

A handwritten signature in cursive script, appearing to read "Valerie L. Hayes".

Valerie L. Hayes
Legal Counsel
Director, Internet & Check Services Program
ACA International
(952) 928-8000 x 103

cc: Gary D. Rippentrop, ACA CEO
Rozanne M. Andersen, ACA General Counsel
Mark E. Davitt, ACA President-Elect
Internet & Check Services Program Committee